

MINUTES
REGULAR MEETING OF BOARD OF LAND COMMISSIONERS
July 17, 2006, at 9:00 a.m.
Room 303 State Capitol Building
Helena, Montana

PRESENT: Governor Brian Schweitzer, Attorney General Mike McGrath, and State Auditor John Morrison

ABSENT: Secretary of State Brad Johnson

VIA PHONE: Superintendent of Public Instruction Linda McCulloch

Mr. McGrath moved for approval of the minutes from the June 19, 2006, meeting of the Board of Land Commissioners. Seconded by Mr. Morrison. Motion carried unanimously.

BUSINESS CONSIDERED:

706-1 FWP – STOCKSTAD AND DAVID FEE ACQUISITIONS
(Ninepipe Wildlife Management Area)

Glen Erickson, FWP Field Services Division Administrator, said I'm here to request the Board's approval of the acquisition of the 70-acre Stockstad property and the 65-acre Davis property, both of which adjoin our Ninepipe Wildlife Management Area in the Mission Valley. This is a high priority acquisition for the department and it is well supported by many rod and gun clubs and other clubs in the area. The acquisition price is \$350,000 for the Stockstad property and \$325,000 for the 65-acre Davis property, both of which would be purchased with Habitat Montana dollars, which is portions of hunting license fees. The area is important upland and wetland habitat within a complex of land protected by private landowners, state, federal, and tribal governments for wildlife conservation, hunting, birding, and related recreation. We've worked closely with the Confederated Salish and Kootenai Tribe and Tribal Wildlife Program as well as the Flathead Reservation Fish and Wildlife Board which approved that in the spring as tentative. Also the FWP Commission gave final approval for this acquisition on July 13, 2006. We had a hearing in Ninepipe Lodge in Charlo, Montana, on July 11, 2006. We received all positive comments from the public, both written and in verbal form. As I said, this is well supported by groups such as Mission Valley Audubon, Five Valleys Audubon, Mission Valley Pheasants Forever, North American Versatile Hunting Dog Association, and others. With the Board's approval today, we will move forward with this wetland acquisition. The key point about this is we will be able to restore approximately five additional wetlands in this area and probably be able to increase the hunter use in the area by 300 – 400 hunter days. Mr. Erickson requested approval.

Motion was made by Mr. Morrison to approve the acquisition of the Ninepipe properties. Seconded by Mr. McGrath. Motion carried unanimously.

706-2 LAND DONATION FROM THE ESTATE OF ANTON SIR, JR
(Benefits: Mt School for Deaf & Blind; Mt Developmental Center; Mt State Hospital)

Ms. Sexton said the estate of Anton Sir, Jr. has proposed to donate approximately 2,599 acres of ag and grazing land situated in Prairie County to the State Board of Land Commissioners to be held in trust for

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Pages 2 through 12 are unrelated to Otter Creek and excluded from this file.

Otter Creek discussion begins on page 13, and is Informational Item 706-11.

Court Justice Jim Regnier to mediate a proposed resolution of this matter. I would add that for the very first time Jim did a mediation with a waiver of mediator confidentiality. We opened this up to the public because it looked like there might be a quorum of the school board present and we did not see any reason why two public entities should not conduct a mediation in public. It turned out we were one short of a school board quorum at any given time in what was about an 8-hour session. But in looking at all of the different legal issues and frankly, in the interest of avoiding litigation between two public entities which we really wanted to do on both sides, we reached a proposed resolution of this particular matter. The title of the land is actually in the school district name which is appropriate we think because after all they made the mortgage payments for 21 years. The property was recently appraised at \$550,000 and another \$240,000 was paid for the malfunction-junction solution right-of-way on that property. The Regents have agreed and the school board has agreed that 30% of all of the proceeds of the malfunction-junction sale plus the appraised value of the property would be a fair and equitable division. Thirty percent coming to the University System and the rest going to the school district. I'd like to thank the department for all the cooperation we received both on the antiquities and the environmental assessment work and I think that expedited our ability to bring this before the Board today.

Motion was made by Mr. Morrison to approve the Homevale Property Settlement. Seconded by Ms. McCulloch. Motion carried unanimously.

INFORMATIONAL ITEMS

706-11 OTTER CREEK

Governor Schweitzer said this is our continuing discussion of the Otter Creek tracts. We've asked the department and others to give us an update on where we are.

Ms. McCulloch disconnected from the conference phone call at this time. Mr. McGrath said he had an appointment and would leave the meeting a little early and miss some of the Otter Creek discussion.

Ms. Sexton said Monte Mason from our Minerals Management Bureau has an update on the evaluation that is being done in partnership with Great Northern Properties.

Monte Mason, DNRC Minerals Management Bureau Chief, said when we met last month I talked quite a bit and I'll be very brief this morning. I know Evan Barrett has some information he wants to provide and Chuck Kerr is here. The primary information I have is the study we talked about last month is complete and the ink is dry. We are putting this together, updating our data disks and getting it out to everyone on our list, the companies and the people that have expressed interest. We are going to talk with them and get a handle on this new information and eventually be back with the Board to have some serious discussions. The study was prepared in coordination with Great Northern Properties and they ended up paying the lion's share of costs. Briefly, I have some background slides that would be helpful for any discussion that might take place this morning. Mr. Mason showed the following slides for discussion: vicinity map, coal resource map (50 mile radius), coal resource map (15 mile radius), Otter Creek coal resource map, Montco-Bridge Creek-Otter Creek Areas map, Tongue Rive Railroad map – proposed spur into Otter Creek, Tongue Rive coal and transportation exhibit, and MT-WY Powder River Basin mine and rail infrastructure map.

Chuck Kerr, President Great Northern Properties, said what I'd like to accomplish today is to give you an Otter Creek perspective from the other half-interest owner, Great Northern Properties (GNP). I know

there has been a fair amount of discussions and publicity about the development of Otter Creek in the press and in our opinion Otter Creek does need to be developed. We think it is an absolute wonderful resource and, frankly, is probably the best coal reserve in the Powder River Basin bar none. It has challenges, however. What I'd like to do today is talk about Otter Creek through GNP's eyes. First and foremost, a bit of history.

Great Northern acquired the Otter Creek property as well as other significant assets from Burlington Northern Railroad in the early 1990s. This was a multi tens-of-millions dollar transaction. We purchased these properties from Burlington Northern and ended up acquiring five million mineral acres, 2,000 surface acres under which is about 20 billion tons of coal. Otter Creek was a substantial part of that transaction. We paid up front for our participation in Otter Creek. The state obviously acquired its interest in the mid-2000s by virtue of the land swap with the Crown Butte Mine, and it was a marvelous transaction for the state. Frankly, the way we look at this is that it removed somewhat of an impediment to us and that was the federal government. We would much prefer to deal with the State of Montana at Otter Creek or anywhere else rather than the federal government due to the fact that anytime the federal government is involved, you just add a lot of time and red tape. The other nice thing about the State of Montana is I think they are aligned with GNP. Great Northern Properties has no coal in Wyoming. Our economic benefit is derived solely in Montana. We do have some North Dakota coal but it is not competing with the Otter Creek type coals. Great Northern Properties is in Montana to do one thing and one thing only and that is to get its coal reserves developed. That is all we do. We are very focused. We have paid dearly for this asset and unfortunately it hasn't developed as quickly as we had envisioned. We think that now is the prime opportunity to move that development forward but it has to be done prudently and, we believe, in concert with several different other factors that have to be taken into consideration. There has been a lot of development work that has gone on behind the scenes. The study Mr. Mason referred to has been long in coming. It was actually dovetailed off a study GNP did in the mid-1990s. We spent a lot of money understanding what resource we had. The mid-1990 study took about 100 years of data, culminated it, and came out with a proprietary study to give us an understanding as to what the Otter Creek resource was. After the State of Montana acquired the property it appropriated \$300,000 and in my opinion used the money very well. It went out and acquired new coal data and cultural studies. What we did was took the brand new data and collated it with the other data Great Northern had to see if there were any new anomalies or new information we could glean out of the new information. In fact, we learned a lot. The old data we had was not acquired using modern technology, the new data was. Probably the single most important aspect of the report is the fact that we learned a lot about the quality of the coal that we have. We have an absolute wonderful resource in that Otter Creek has 1.2 billion tons of coal, the state owns half and we own half in an extremely low strip ratio that has one unfortunate aspect to it and that is it is high in sodium. The fact that it is high in sodium is a significant issue and unfortunately does not lend itself well for being burned in conventional boilers. It causes boilers to slag. So there is a market issue there. We've been working with the DNRC with regard to the study, discussions about how a lease process would proceed. What sort of process would be required? What sort of lease would we have? What sort of lease terms would be in place? All of these things have been going on behind the scenes, so a lot of work has been going on even though it appears no development is taking place. Lets talk about the challenges we face on a "go forward" basis.

Challenges: Otter Creek has one problem of which all of the other problems are derived. It is location. Otter Creek is obviously a remote area. It is in a geo-politically sensitive area. You have the Northern Cheyenne on one side, who are an active participant in this process and you have the Custer National Forest on the other side. It is in an extremely rugged area. You have the Tongue River running through it. It is a pristine area. All of this is going to be an issue with regard to the future development and needs to be taken into consideration. At present, there is no infrastructure. There is no rail, there are no

transmission lines, and there is no pipeline there. So anything that needs to be done has to be built and somebody has to pay for it. The fact that we do have a different coal needs to be taken into consideration. Unfortunately, high sodium coal is not in high demand. The market is very finite. The southern Powder River Basin right now is mining and selling over 400 million tons of coal per year. The high sodium market is 20 million tons per year. So, that is the market we are looking at. Even though we have a wonderful resource you have to look at what you can do with the coal if you dig it out of the ground. Right now that market is being fed by Spring Creek, Decker, and another mine or two. So in order to break into that market you will have to either displace that market or figure out a way to handle sodium. Sodium can be mitigated in a couple of fashions. One is to blend it with other coals which adds cost. Another is, we think, that technology may have some intrigue here.

Economics: To build infrastructure in this neck of the woods is going to be very expensive. Obviously, the Tongue River Railroad folks have worked very hard over many years to try to get a rail built in here. It's Great Northern's opinion that they are on to something. The problem with the rail, however, is that in recent times the cost of construction not only of rail, but power plants, and coal mines has increased substantially. What used to be the rule of thumb of a million dollars per mile of running mile of rail is now in this particular case four million dollars. You're looking at almost \$500 million to build the Tongue River Railroad from Miles City down to Spring Creek-Decker. That is going to have a substantial impact on the ability to get this done. Mine costs have gone up substantially. In order to open up a brand new mine we're looking at anywhere from \$150 to \$200 million of funding capital to get a mine of this nature opened up. So you're looking at anywhere from \$600 to \$750 million to get Otter Creek developed. If you're having to pay that kind of money to get the mine open and you have a very limited market, we're really concerned about economics. We are working very hard right now to understand the economics and make sure that whatever we do is economic. That's one of our primary focuses. The fact that we don't have rail is probably the single issue we have in getting Otter Creek developed. We believe that the rail and the coal need to be developed in conjunction with each other. You can't sell coal without rail and rail is going to need coal to be able to have an anchor tenant to help pay for it. The Tongue River Railroad folks have proposed a common carrier line that goes from Miles City, Montana, down to Spring Creek-Decker spur and would connect with the Burlington Northern-Santa Fe line. They have been working on that for 20 years and I know there is some concern that that may open competition from the south across this track. We, as Great Northern, have been concerned about that as well, the fact that we do not have any economic interest in Wyoming. Obviously, we are aligned with the State of Montana, however, in looking at this closely what we believe is that line will actually be a benefit to the development of Otter Creek, to the State of Montana, and to Great Northern not only for Otter Creek but for other opportunities as well. There is going to be other industries built in Eastern Montana that can utilize this line and we believe, structured correctly, we can make sure Montana is adequately protected and, in fact, there may be an opportunity where we can have the Wyoming developers pay for part of this line. They will use this line to ship their coal across it and we believe there is a price to be paid for that. So we think Wyoming coal can help pay for Montana rail.

Low Strip Ratio: The endearing quality of Otter Creek is such that it has a very low strip ratio. Its cost of mining will be lower than any other mine once it is opened up. It is going to take probably six to eight years before the first lump of coal will be mined out of Otter Creek. That is being aggressive. In six to eight years all of the Wyoming mines will get into the higher strip ratios. Their cost of mining will go up. We believe that Otter Creek alone will be competitive. We also believe that due to modern technology sodium will be taken care of, new plants will be built and designed that will be able to handle high sodium. There is a company owned by one of the limited partners of Great Northern that has a fix today that can retrofit existing boilers to be able to handle high sodium and it is relatively inexpensive. We

think there is a package that we can put together to be able to break into other markets other than high sodium. So we think that technology will advance.

Relationship Issues: The Northern Cheyenne are a player in this, they have reserves of their own. Otter Creek is right next door and anything we do is going to impact the reservation. We believe it is important that the relationships are solidified as a foundation for any future development of this area. There are locals and the national forest. It is the relationships that are going to make this work. It's the backyard issue, you either want it or you don't. Frankly, we are here today to try to get Otter Creek developed but if other factions don't, fine. We've got other resources in Montana that we are working really hard to get developed and we will continue to do so. However, this really is a tremendous asset for the State of Montana and Great Northern.

Economics is a critical element in all of this. If we economically can't mine and rail out the coal, then we're gone. With the current capital costs we are really concerned that it is going to be too expensive to get all of this done. We don't have the answers to the economic questions at this point. We are working hard to get them. We are working in conjunction with the Tongue River Railroad folks to assist them in getting their rail developed. The last update I had is they expect to have their permit issued in the third quarter of this year. The last remaining issues with regard to concerns about the rail have been satisfied and the STB will issue a permit sometime in the third or fourth quarter of this year. The common carrier line is one option. We believe it is a beneficial option. I know there are other options that we may be able to build rail from Otter Creek to the north or from Otter Creek to the south. Those will have to be investigated. There is a lot of moving parts and at this point in time I think it is a matter of information gathering before we're ready to go to a lease offering. In my opinion the path forward is one of information gathering, but I think it needs to be done very quickly. We're in an economic boom for coal. Right now in the high commodity-priced environment with natural gas at \$6 or \$8 per NCF or prices at \$70 or \$75, coal is a cheap fuel and there are plenty of opportunities and alternatives for the use of coal. The phone is ringing off the hook in Houston, people looking for sources of fuel and we think we can provide them. The challenges we face with Otter Creek is its location. We think those can all be mitigated but we have to walk before we can run. We think we need to have a full understanding of the economics. That's happening very quickly. We think in the next month or so we should have a better handle on mine and rail economics. Then we can back into how many tons do we have to sell in order to make all of this work. That will help size the mine. Once you have all of that then you can determine finance-ability. Obviously, to finance a mine you are going to need lenders. To finance a rail you're going to need lenders. We need to make sure this is going to be economic and we can get this thing financed.

Market Research: If you have a very finite market, you better understand it. Where are those markets and can we break into them? If we can't then, again, it's a potential fatal flaw. So we really need to understand the markets. Before you ever open up a mine you will have long term finance-able contracts to be able to go out and obtain financing. That's the way mines are opened up.

Transportation: It needs to be figured out. In Great Northern's opinion we believe the Tongue River Railroad is a wonderful solution. And we are willing to back it. We think that it provides the opportunity to develop Otter Creek as well as other opportunities in Eastern Montana. In fact, if you can solve the sodium issue, maybe technology will do it or this technology that this company has will work, then that rail going south we can start working on not just the finite sodium market but the market that the other PRB mines are selling into. If we've got a lower cost of fuel we can be competitive if we can solve the sodium problem. So having access to the south as well as to the north we believe is very important. The state needs to understand what it wants to do in that regard. If it wants to support the Tongue River

Railroad it needs to answer that question itself. We, Great Northern Properties, are interested in looking at all avenues in that regard and haven't yet made a decision. We still believe the Tongue River Railroad provides a very compelling solution to that issue. The DNRC and GNP still need to work together on formulating a lease that is going to be satisfactory to all of us. One of the concerns I have is if you have a lease auction the people who can pay the most may be those people that don't want to have Otter Creek opened up, the potential competitors to the south. So what we need to do is structure a lease that we believe will have significant development hurdles to make sure that whoever is going to lease Otter Creek pays a significant price for that development in the event they lock. That we get something for it. I want to make sure that whoever leases Otter Creek is real.

Focus on Relationships: Great Northern and the state have a great relationship. I want to leverage that into a wonderful relationship with the Northern Cheyenne and the locals. There are a lot of farmers and ranchers in that neck of the woods that are going to have a say in this as well. You've got the Custer National Forest and the markets. We think the relationships have to be worked together all at the same time.

In summary what I am saying is there is a lot of work to do. At this point in time I don't believe GNP would be in support of putting its coal up for lease. We believe additional work has to be done so that as far as GNP is concerned, we maximize the value of what we have to our shareholders. Again, we paid our price up front. The State of Montana has been blessed by having this as a wonderful asset. It will get royalties, it will get tax dollars in the future. GNP will get the royalties, but we won't get the tax dollars so we have to make our best deal on the front end. We are very focused on maximizing that. To the extent that I'm here representing my shareholders, you are here representing the school trust lands and we both have a fiduciary responsibility to maximize the value of Otter Creek. In GNP's opinion we believe we are on the right track. We think in the not-too-distant future we will be ready to make a recommendation as to what we do with Otter Creek, but not yet. We think we need a few more facts before we can make that decision.

Mr. Morrison said Mr. Kerr, you mentioned the northern route from Miles City to Otter Creek is one option that has been discussed and needs to be looked into further. You also suggested you strongly prefer the southern route being developed as well. My question is whether just a northern route that goes from Miles City down to Otter Creek is consistent with developing this in the long run. A lot of the opposition to the Tongue River Railroad is related to (1) the competitive issue, but (2) the impact in the area around Birney in the Tongue River Valley. So, what about the northern route only on the Tongue River Railroad and is that consistent with future development?

Mr. Kerr replied it may be. The issue is going to be twofold. One, economics. If you're going to put a short line railroad in that is serving only one customer it loses its common carrier status. So we won't have other people helping finance that rail. So the mine itself will have to finance 100% of that rail, or any other developers of coal in that area.

Mr. Morrison said but it is a less expensive railroad.

Mr. Kerr said it is a less expensive railroad but 100% of the cost will be borne by the mine. The fact that this is a common carrier line has several significant advantages. Probably the most is it gets the right of eminent domain. When you apply for a permit at the federal level, you have to demonstrate a need. Being that this is public access, which you are demonstrating, it is a need for the public good. You only have to demonstrate that need once. And if you are successful in demonstrating that need you are granted a permit. Along with that permit comes the right of eminent domain for the entire length of the rail. But

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it has to be for the public good. A short line railroad is not for the public good, it is only for one person. In order to acquire right-of-way access you have to demonstrate need across each individual track as you go and you will be in court for many many years trying to demonstrate need as you go. So there is a different permitting process. Secondly, the economics. The short line rail, the coal mine will pay 100% of that and will be given favorable loans from the U.S. government. A common carrier line will have available federal loans from the U.S. government at very good interest rates. There is a loan program, I think it is the Railroad Infrastructure Loan Program or whatever, that has a common carrier line. You have access to cheap financing. In our opinion the competitive side of this, we believe that competition from the south can be mitigated. We believe that is not an issue to short cut not going to the south. In fact, if we can solve the sodium problem we are going to want access to the south. Cutting off that distance will help our transportation costs such that we can be more competitive. So it is a double-edged sword.

Mr. Morrison said my other question is about the Northern Cheyenne settlement. A couple of years ago the Northern Cheyenne had a suit that was pending that this Board settled with a settlement that provided for certain stipulations in the event of future development. And my question is whether that settlement creates any kind of impediments for development at this time, in your view?

Mr. Kerr said I don't think so. We've done a significant review of the settlement agreement. It's a cost. But if you were to locate this mine anywhere near a population center or anywhere else I think there is a cost of doing that too. You're going to have to take into consideration your impact on the local area. What the Northern Cheyenne have asked is they are going to be impacted that we take a look at mitigating those impacts to the extent that they have some sensitivities, they've expressed them and we believe those are reasonable and sensible. Historically, with development of mines around reservations this sort of agreement is in place. We don't believe it is an impediment. Again, with the fact that you have such a huge reserve, 1.2 billion tons in one spot with a very low strip ratio, we believe the economics and this resource will be able to absorb the settlement agreement without significant concern.

Mr. Morrison said there have been some people who suggest the reason Otter Creek hasn't been developed yet is because of that settlement agreement, and you're confirming that is not true. The settlement agreement does not create a significant impediment and these other issues in terms of making the financing pan out and getting the railroad in place are the critical components.

Mr. Kerr replied absolutely. In my opinion the two issues are infrastructure, lack thereof, and sodium. Those are the two issues why Otter Creek hasn't been developed, or that you haven't seen any other development in the sub-bituminous coals in Montana. For whatever reasons, if you go north out of the southern Powder River Basin the coal character changes, and it's right on the Montana-Wyoming border. You get north of that and all of a sudden the sodium levels increase, and the sodium creates significant problems in conventional boilers.

Governor Schweitzer said you mentioned relationships. I think that is important. That relationship between the Northern Cheyenne and the State of Montana and Great Northern is one that we'll continue to work on. For many of you, you don't know that Chuck Kerr actually came in to see me before I was sworn in, but after I was elected our first meeting was at a card table in the Rotunda. Chuck arrived, as a lot of folks do, with a lobbyist. And I said Chuck you don't have to have a lobbyist to get in this door. We scurried him right out of the Capitol and we've had several meetings since. It is kind of a new way of doing business around here. For those of you who are lobbyists, its okay to be a lobbyist but we're saying to people you don't need to hire one to come and talk to us. We've had a great number of conversations about new technologies relative to coal. And I think Great Northern Property has done more exhaustive

research project on emerging coal technologies of coal gasification, liquefaction, than almost any other company in the world. There are those that have suggested as we develop coal in Montana it will be coal by rail, traditional. There are others that say because of the unique nature of some of Montana's coal it might be good to look at other technologies. If you may, I'd like to address what you've found in emerging technologies in terms of gasification, liquefaction, IGCC and what the possibilities might be for those coal assets you have in Montana. Not just Otter Creek but other assets you've got.

Mr. Kerr said Great Northern Properties is the single largest owner of coal reserves in the United States, other than the U.S. government, by a far stretch of the imagination. We have on our books 20 billion tons of coal. The next, number two, is Peabody Coal that has nine billion tons. The difference there is our 20 billion tons is owned. We own it in fee. Peabody's is leased for the most part, they do have some fee coal but obviously our coal is here in Montana. So we have a very vested interest in anything that can be done with coal, regardless of what it is, we are going to take a keen interest. It would be foolish not to. That's why we are so enthused about monitoring current technological developments. There has been some really intriguing stuff that has gone on recently. You have to understand the reason this hasn't taken place sooner is commodity prices. A lot of these new technologies are not economic when you have \$2 and \$3 gas and \$20 and \$25 oil. It is only recently, the past two or three years, that commodity prices have gone up and people believe those are sustainable prices, that these technologies have been rolled out and are not economic. There are several types of technologies that we believe can be developed in Montana in concert with each other but they basically all use one concept: the gasification of coal. You take coal, you run it through a chemical process instead of burning it and you convert the coal to a synthetic gas. Basically, all you're doing is rearranging the molecules to get to the basic elements you can use to convert carbon and oxygen and hydrogen into whatever product you want. Synthetic natural gas can be made from the gasification of coal. Diesel, jet fuel, methanol, there is an incredible product stream. Once you end up with synthetic gas you have a product slate that is just remarkable. You can take the synthetic gas and put it into a combustion turbine and burn it and convert it to electricity. All of these can be done with Montana coals. What is really critical here is the majority of Montana's coal are lignites. What we've been talking here is sub-bituminous coal which is higher BTUs, can be dug out of the ground, put into rail cars and shipped and exported. It can also be burned on site or utilized on site. Probably the highest and best use for sub-bituminous coal is for export. Lignite, however, being a lower heat value, even a lower ranked coal, transportation costs make it very difficult to compete against the higher ranked coals. Lignite is chemically unstable. If you dig it out, put it into rail cars, as it travels it settles and it will start self-combusting so you end up with trains on fire. You've burned your coal before you even get there. The reason you haven't seen massive lignite development is it is going to be mine mouth. What you need to do is dig the lignite out of the ground and put it into a facility and process the coal on site. That is what North Dakota does, that's what you see in Texas or anywhere else where there is massive quantities of lignite. Historically, it has been dig it out of the ground, put it into a coal-fired boilers, burn it, it converts to steam, and fire steam-fired turbine generators. With the new technologies however, we believe coal will be gasified and turned into all sorts of different types of products depending upon where your markets are, what you need, and what the commodity prices are. Unfortunately, most of these technologies are playing catch-up, most of these have been around for a long time but haven't really been perfected because they have been on economics. For the past two or three years everybody is trying to get them geared up. But they are very capital intensive and its going to take some time. So while we all talk about IGCC and coal gasification its not necessarily ready for prime time. I think its going to come, there is going to be projects built all over the U.S. with the new technologies, its just going to take some time. Our coals lend themselves only to a very select group of technologies. The technologies you hear about, and they are name-brand companies: G.E., Shell, Conoco, Phillips, their technologies are designed for the higher-ranked fuels and don't lend themselves well to the low ranked fuels. So those technologies won't work on the majority of Montana coals. We've identified those technologies that do work and are

focused on trying to get those technology-providers focused on Montana. I think we've been doing a pretty good job behind the scenes. Great Northern is spending the majority of its time and effort on the new technologies and we believe that is the future for us and we believe it lends itself well for the State of Montana. The new technologies are much more environmentally-friendly, they are CO₂ capture-ready and we believe CO₂ is a wonderful story for Montana as well. Montana has oil and gas reserves that will lend themselves for recovery using CO₂. Montana has it all. It has a wonderful resource, it has more coal than any other state in the U.S., it has an administration that is supporting the development of coal, and we're here. We can't move the resource so we're here to do what we can with what we've got and we are working really hard in that vein.

Governor Schweitzer said one other thing, we own Otter Creek in a checkerboard fashion in partnership with Great Northern. We've looked at a number of your other assets around the state Kinsey, West Circle up Nelson Creek, and in some of those cases you are checker-boarded with the federal government. There are a couple of ways of looking at the Otter Creek tracts. One is we need to get infrastructure in to the Otter Creek tracts in order to develop that coal. The second might be moving the ownership of the coal to a place where there already is some infrastructure. Can you give us some ideas, some sort of things that might potentially exist?

Mr. Kerr said absolutely. As stated earlier, one of the wonderful attributes we believe Otter Creek has is the co-ownership with Great Northern Properties as a privately-owned company with the State of Montana. The federal government had it for many many years and basically did nothing with regard to the development. The development was being done by Great Northern Properties. The State of Montana, however, is very focused in the development and we'd much prefer to do business with the State of Montana because they are financially lined with us, are focused on getting something done and I think have the same mind-set for business development that we do. The federal government has none of that. It creates tremendous dissention or inopportunity for quick development of coal in Montana. Any time we deal with the federal government we add two to five years from the timeline that we would be doing prudent development with the State of Montana. So, to the extent we can deal with the State of Montana anywhere we have significant reserves we'd love to be able to do that. We would be very interested in facilitating discussions with regard to swaps where we can block up an area where there is federal coal intertwined or checker boarded with GNP coal. We believe that is a win-win for the State of Montana as well as GNP. GNP has already initiated the process of a federal land swap. We do have a fair amount of acreage that is already stranded in the Custer National Forest and we believe we're going to be able to attempt to swap out some federal acreage elsewhere. But we also believe there is a bunch of state acreage that can be done the same way. To the extent the state is interested in partnering up with GNP and putting together a areas of interest we'd be all over that.

Governor Schweitzer said just to recap, what you said to us is GNP doesn't believe, as our partner, that we are in a position to be offering these assets for lease right now until the path to infrastructure is clear and the value of that coal has been enhanced because of that path?

Mr. Kerr said that's correct. We could lease today but if you were to lease, who would show up? And who would be willing to pay any significant amount of money for something that has no infrastructure, that doesn't have the relationship solidified, and has all of the work we've got to get done? They are faced with all that. I don't think they are going to give you much money for your coal. Frankly, GNP is here to maximize its reserve to the benefit of the shareholders. I think the Land Board has the same fiduciary

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responsibility to its constituents. At this time I think we have to do a lot more work to not only figure what the process is going to be but what routes we have to take to get there. We have the relationship issue again, the transportation issues, and the market issues. All of those have to be resolved or at least understood so we make an informed decision on when we put this up for lease. I think now what you're doing, and I mentioned this to you, you're running a K-Mart "blue light special" and you're giving value away that I think is value that can be put into the coffers of the school trust fund and GNP.

Governor Schweitzer said you made a comment and I want to clear it up because it is something we've talked about and I've talked about other folks who are interested in the Otter Creek tracts as well, and that is if we were offered the lease right now, the ones who could pay the most for it probably are big miners of coal in the Powder River Basin in Wyoming to make sure that those tracts were not developed.

Mr. Kerr said that is a significant concern of mine, yes.

Governor Schweitzer said the next one, just to recap, GNP believes the new technologies coal gasification and the derivatives thereof have great potential in the intermediate term future in Montana?

Mr. Kerr said that's correct. One thing I didn't state is Otter Creek is an absolute wonderful reserve. In my mind the highest and best use is as a mine only. Not as a mine-mouth facility. At some time in the future you may be able to put a mine mouth facility there but I think there are too many hurdles and there are better uses for the coal. If you have rail moving a project, a coal-to-liquids project, a gasification project, closer to infrastructure where you have it closer to Miles City or in that neck of the woods, I think that is going to be easier to do than trying to put a mine mouth facility in Otter Creek. So, it is GNP's belief that highest and best use for Otter Creek reserve is a mine only and would be for export purposes.

Governor Schweitzer said the last thing is there was a discussion you made about the potential for swaps which would mean, hypothetically, if you had a gasification project-liquefaction project on one of your other properties someplace, you'd be interested in Montana being a partner in that in terms of coal. You would have the federal government trade into Otter Creek and Otter Creek tracts trade into property that is adjacent to your property and then the development of property in another place in Montana could be conducted based on the swaps out of Otter Creek.

Mr. Kerr said absolutely. GNP has 60 identified deposits that can be developed. Otter Creek is one. Obviously, Otter Creek has high value. But that is not the only project we are pursuing. We believe there are other projects just as compelling as Otter Creek that have different virtues. We are very interested in doing that. So to the extent that we may not be able to get the Otter Creek developed some time soon, we think Otter Creek will be developed and we are in it for the long term. The owners want their kids, grandkids, and their great grandkids to be able to partake in the GNP legacy. In the near term, however, we think there is tremendous opportunity in this economic environment. We don't know how long that window of economic opportunity will remain open. To the extent that we can develop a relationship with the State of Montana that provides for quicker economic development, by all means we are all for it. To have the State of Montana as a partner in a project development of this magnitude is a wonderful asset in our book.

Eugene Little Coyote, President Northern Cheyenne Tribe, said my Cheyenne name is Maya-nahun. I'd like to share a few comments on the Otter Creek Settlement and potential development there. I'll keep my comments fairly general, but I would like to introduce members of our delegation. We have Tribal

Councilwoman Judith Spang and Tribal Secretary Sharlene Evans. Let's begin with a simple background as far as our two shared administrations go. After your inauguration you invited the Northern Cheyenne Tribe to a government-to-government consultation in which we had an exchange of ideals, initiatives, and issues the Northern Cheyenne Tribe and the great State of Montana shared. During this meeting you presented the Northern Cheyenne Tribe with a potential opportunity regarding the Otter Creek coal mine or coal development. The Tribe's immediate response was that as far as the Otter Creek Settlement goes, it was settled. We had sued on our claims regarding the negative impacts of Otter Creek, but we settled that and dismissed it with prejudice meaning we can't sue any more over it. However, there was some like discussion about the potential of the Northern Cheyenne Tribe and synergy. But if Otter Creek is going to go forward and the Northern Cheyenne tribal people want to develop their own coal it could be a very great partnership. That was too early for us to really comment. The comment we had made to the Governor's office was that that kind of decision is much too big for the governing body alone, it would have to come from a vote of the tribal people. Governor, of course, you respected the Tribe's views on that and you were very patient. One of the things I am here to share with you today before the Land Board is that a significant number of Northern Cheyenne tribal members have petitioned the Tribal Council for coal development. The Tribal Council took action to approve putting this as an initiative vote on the November staggered elections of the Tribal Council. So in November when we elect or reelect Tribal Council members, the tribal people will also decide whether they want to move forward with coal development. Now what this does, of course, is if it moves forward it puts the Tribe in a very good position to help both the state and itself on a number of things. I do want to add a couple of things before I get too far. One, I was told by the Tribal Council to emphasize the governing body by taking this action to put it up for a vote of confidence for the people isn't necessarily supporting coal development. What they are doing is supporting the tribal people's rights to decide if they want coal development or not. Secondly, this definitely activates a number of conditions in the Otter Creek Settlement Act. I'd like to just point out four of those. One, by dismissing all of our claims with prejudice it allowed the transfer of Otter Creek tracts to the state for potential development; and two, in return the Tribe would get 8.5 sub-sections of sub-surface rights on our reservation, so that was a good thing for us, from Great Northern Properties. Also, two other things we've consistently mentioned to the State of Montana is that this settlement had a condition with it, that a Montana Congressional delegation would in the promptest manner seek federal funding for aid, about \$6 million per year, for the Tribe's own infrastructure, roads etc. but also funding for our cultural programs.

I know you posed your question about if the settlement is an impediment. Well it is a settlement and it allows things to move forward. But there are some conditions to it and that is what I am also here to express. We would hope that Montana lives up to its conditions as well. I'll read Recital G from the actual settlement which I have here. It states, "The Tribe advises that in its view realization of these settlement objectives will for the first time provide the Tribe with a net positive stake in nearby off-reservation coal related development and therefore generate Tribal support for coal related development at Otter Creek carried out in accordance with applicable law." So, I would like to conclude my brief comments saying that we want a "net positive stake" in this development if it moves forward. What that does is it supports the Tribe's own vision of economic independence. We've had actual consistent discussions for the past year and a half between our two governments on this matter, I appreciate that. So, I am inviting the great State of Montana and Great Northern Properties to renew meaningful objective discussions regarding the conditions in this agreement and also to have more discussions on realizing the tremendous opportunities that Otter Creek presents.

Mr. Morrison said just so its clear, I was a supporter of that settlement and I raised the question with Mr. Kerr because in the course of political debate there had been some who claimed the settlement agreement we entered into with the Northern Cheyenne was the obstacle to development of the tracts and I wanted to get his perspective. I was glad to have him say here today on our public record that, in fact, this settlement agreement is a constructive thing and it is not an obstacle to the development of Otter Creek. So the fact that we have been able to enter into this settlement that creates a net positive situation for the Northern Cheyenne Nation is a good thing.

President Little Coyote said he agreed.

Representative Jim Keane, HD 75, said in listening to the discussion I have some comments while they are setting up the power point. The comments I think need to be made here is Montana is a resource state and we all know that whether it is tourism, fishing, hunting, farming, mining, or oil and gas, its all resources. Sitting in this room if you look at Lewis and Clark there has been a consistency for over 200 years, and while Lewis and Clark came here everybody forgot why they came here. They came here for transportation. And what got them through their whole mission? If they couldn't have traded for horses, they wouldn't have survived. When we talk about our resources, they have no value. Our resources in this state have no value without transportation. Whether it be tourism, mining, or agriculture, transportation is the key to everything and I think sometimes as a person in transportation we forget that. We're talking about rail today, in my home town at one time we had five railroads. The reason was we were the economic driver of the state and they came there because that's where the transportation needed to be. Things have changed, things move on. There is a unique opportunity, and you heard that discussion this morning, as prices change economic value changes. Our coal now has significantly changed. A person like myself, while I represent Butte, my day job is I represent the operating engineers. In other words, the people that mine coal in Montana, I represent about half the miners for the tonnage. We mine about 20 millions tons per year of coal in Montana so I have a significant interest in what happens to coal and what happens to coal in Montana. Our organization for the past 20 years has been deathly opposed to the Tongue River Railroad and we will stay that way. The Tongue River Railroad does nothing, it is a transportation corridor for Wyoming and people need to understand that. It has nothing to do with Montana development, it has everything to do with shipping coal from Wyoming up to the Northern Tier. It has been that way from the start and it is that way today. I want the Land Board to understand our organization will stay opposed to the Tongue River Railroad because it doesn't do anything for Montana. In fact, the miners I represent I guarantee you the first year they went into operation of the Tongue River Railroad we'd lose about 200 miners in the State of Montana. Because the route becomes so cheap our coal isn't competitive at Colstrip, Colstrip isn't competitive at Sarpy Creek. So we need to be aware of that when we talk about the Tongue River Railroad. Yet, we've heard all the discussion, there is an opportunity. I spent all of January and February down in this country negotiating contracts and I have had people come to me that have a better way. Have a way to solve the problem and protect the jobs we already have. And that's what I am about, protecting the jobs but at the same time developing the resource. This resource will be developed, if not in Montana, in Colorado, in Texas or somewhere else. Do you know why? If you go back five years and look at what Burlington Northern invested in coal hauling equipment – zero. Four years ago – zero. Then they started investing. Last year coal-hauling engines and coal cars – \$500 million. Tell me the private company is going to put up \$500 million and let them sit on the track. They know what everybody else knows, there is all kinds of development in coal because, you've heard it this morning, it has become the best economic fuel we have. So, you have \$500 million and those coal cars are going to be full with somebody's coal, I want it to be Montana's coal. I think the citizens of the State of Montana and certainly the Land Board and this administration are trying to move towards that. So, how do we get Otter Creek developed? How do we listen to Chuck's concerns about getting fair market value for their stockholders? How do the citizens of

Montana get the best rate? I think these people have come up with a solution to all our problems and my problem, we still protect the jobs.

Transportation – Otter Creek Coal. He showed a slide of the proposed Otter Creek route, saying the Northern Cheyenne is next to it and you can see the Tongue River Railroad running next to it. Here is where we want to go with the shipping of the coal down to Decker. Straight southern route. That's what we need to do. These numbers come from the EIS for the Tongue River Railroad and they will have to be updated as we go along. Why do we think the southern route is an advantage? On the southern route there is just about 1/3 of the railroad line, it doesn't get involved with the northern part at all. We go down to Decker, what does that get us? It gets us to ship our Otter Creek coal into the eastern railroads where the Dakota, Minnesota and Eastern Railroad and that other one that is part of their system over there off the Burlington Northern line. So we are able to move our coal south, Governor, we protect our coal going north out of our other mines and we're into all of these new markets down south with the Otter Creek coal. As the discussion talked, this gets the blending of the other coal which our coal can be attractive for whatever the lease price is to blend with other coal coming out of Wyoming. Why would they do that? Because if it is at a decent price they are going to want to do that. So how does this work out? The southern route contacts with the DM&E and eastern markets. Here is the business approach. Build a branch line to Otter Creek south, move coal down to BN-SF at Decker, move coal onto the other lines through Burlington Northern, and allow a branch line to run on the tracks. In other words what you do here is, all they will do is build a railroad, then Burlington Northern can run on their line with their trains, with their engines or anyone else who wants to haul coal. How do they get paid? Dollar a ton to move the coal over the 41 miles south. Profit reinvested in Montana opportunities. Here is their business plan and this can be adjusted. Ten million tons the first year, 12.5 the second, 15 the third, 17.5, and you heard the market is 20 million tons, that is the current market. I think once we develop the line and are able to ship south that will be our developed market. I think we are going to see an increased coal. If they are buying \$500 million worth of coal cars you can bet power plants or whoever is using the coal will come up with a way to burn it with the technology, or as other assets become available to do other things with the coal.

Debt ratio. We were looking at a debt ratio of 10% equity, 90% ratio. Capital costs is \$73.5 million, that's figuring about \$1.8 million per mile. You heard today it is \$4 million per mile, I think there is going to be a real plan. Supposedly our people are going to work on the Roundup Railroad this year, I think we can do a comparison of what it is costing to build the Roundup Railroad rather than say \$4 million. I think that is a high price. Debt term is 9% at ten years dollar per ton charge, 110 tons per car, about 100-car trains. One of the things that hasn't been mentioned that they are doing in Wyoming is bonding. I think part of that debt could be bonding. That hasn't been talked about today but bonding by the State of Montana. If you need to guarantee part of that debt through the money we have that's coming in through the coal trust I think there should be some discussion about that. Their rate of return over the five years is 21.3%. Tongue River Railroad south, \$1.8 million, that will have to be adjusted, I think we need to take a look at real numbers instead of pulling them out of the air. Here is the cost of 41 miles, about 1/3 of what it is, \$73.8 million. Here is the current proposed costs, this is at \$1.8 million miles on the Tongue River, \$207 million for construction costs, so roughly 1/3. You don't have all the other impacts. Here is the impacts we see on the southern route, and these came from the EIS for the Tongue River Railroad, number of homes – zero, there are about 672 acres affected, landowners affected about 13. So it is a heck of a lot easier to negotiate with 13 people where you don't have to condemn the land and make a deal with just 13 people and there is four at-grade railroad crossings. This rail link should serve the needs of the bidders of the Otter Creek tracts. That is what this railroad and that is what these people who want to build this are all about, just to serve the needs of the Otter Creek coal tract. That's all they would have to do to make the income. And if the Northern Cheyenne want to develop their

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resources, it is a railroad for hauling coal or anything else they want to haul up there. It will also serve the transportation needs if you are going to build something up there. You can't build anything like this without a railroad. So if you were going to build a facility at Otter Creek you need the railroad in there. I would like to state, I was sitting here kind of gritting my teeth on this, Otter Creek is out in the middle of nowhere. Well, I was going to Colstrip when Colstrip was out in the middle of nowhere and people couldn't do it there and for years we had construction jobs down there, for years they built the town, so if it is out in the middle of nowhere and there are some dollars laying in the ground out there, you can build it out there. But it takes a railroad to do that. If you go down to Colstrip and take some pictures in the early 1970s when a couple of guys were kicking around the grass out there and figuring out what is going on and take a look at it today, it is a totally different picture. I say we can develop Otter Creek, not just for the railroad, we can develop it for plants and other things too. Because if you build it they will come. That's the alternative route to market for the coal markets. I want to go on record to say our organization does not want to stop Montana jobs by building a Tongue River Railroad when we can develop this area in a better way, at a cheaper cost, keep our financing, and do a better job for everybody involved.

Mr. Morrison said thanks for that good presentation. Have you looked at doing just the northern railroad instead of the southern railroad and compared those costs and opportunities?

Rep. Keane said I have been approached to get on board with the northern route and I think it is a terrible route for two reasons. There are more environmental impacts and there is going to be tougher negotiations, it goes through different ground. That is the one issue. The other part is, my concern still is if you build 2/3 of this line down there then the Wyoming people might come and build the other 1/3. If we start shipping south down into Wyoming's turf rather than allowing them to come into our turf, I don't support just the northern route, no. Because it gets to the same point. They have developed an infrastructure that can mine ten times the coal we are mining right now. So, why do we want to help them build their infrastructure? They are a cash cow down there that we need to compete with, and we need to compete wisely. The other concern the Land Board and GNP has is just what was stated, I think if you negotiate a lease, whoever you negotiate the lease for the coal for Otter Creek, you have to demand and put a construction time and a mining time in there where someone just doesn't buy it up and say thanks we're going to keep mining down in Wyoming until it gets too expensive and we may mine up here. These people don't develop this railroad unless there is a guarantee that we are going to develop the mining at the same time. It has to happen that way. The long answer to your question is I don't support the northern route.

Mr. Morrison said you're saying if the northern route is build out you think that Wyoming private developers might choose to go ahead and build out the southern 1/3 by themselves and create that link that you don't want to see exist. Whereas if we focus on the southern end, that they are less likely to invest in making that completion on the north end?

Rep. Keane said that's correct. Take a look at it, it is 2/3 longer and the costs go up exponentially to build it through tougher territory with more problems. Our little thing here is \$74 million, you're talking \$150 - \$160 million so why spend that kind of money when we can get better access to an area? The Decker people have the access to coal and the Otter Creek can go south, it could go the other route if the price is right. It can come up through the Billings area and around to Miles City and those are all negotiated freight rates.

Mr. Morrison said does the southern route that you base your cost estimates on go through the valley at Birney there?

Rep. Keane said no, the southern route is a different route.

Governor Schweitzer said we've been talking about building a railroad down to Otter Creek for 25 years, so I guess this is another proposition. The more propositions we have the better chance we will get something built.

Rep. Keane said we need to build something into Otter Creek and I think this takes a lot of the pressure off, it creates more supporters than I believe would be for the entire line. It creates a better economic package and it cuts the costs down that you have to finance. I would certainly like the Board and others involved to start considering this.

Governor Schweitzer said is there anything more on Otter Creek for this go-around? Monte are we going to review the stuff as time goes on and will present more information? That sums it up for Otter Creek.

Motion to adjourn was made by Mr. Morrison. Seconded by the Governor.